

Mediation-Arbitration Clauses

The Importance of Drafting

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I. Introduction

In a recent decision of the Swiss Federal Tribunal in connection with the challenge of an arbitral award,¹ the question came up whether pre-arbitration conciliation (or mediation, as the case may be) is required before arbitration proceedings can be instituted if the parties have agreed on such a mechanism.² The Federal Tribunal - in taking the established facts and the wording of the specific clause into account - agreed with the arbitral tribunal and found that it was not. The Federal Tribunal, however, did not decide on the question of whether such a requirement introduced by the parties affects the arbitral tribunal's jurisdiction to hear the dispute in the first place. This note deals with this question and other problems possibly resulting from such clauses.

The dispute decided by the Federal Tribunal arose out of a contractual relationship between a French developer of automatic machines and other industrial products and a Chinese branch of a group being active in the field of producing household appliances. The contract, among others, contained a clause stating that the contract and all legal relations arising out of it was to be governed by Swiss law. It continued³ that all controversies and all disagreements in the relationship arising in connection with this contract and which could not be amicably solved (including conciliation under the rules of WIPO⁴) should be submitted to an arbitral tribunal which should be competent to definitely decide the dispute, with the exclusion of ordinary courts. It further stated that the arbitral tribunal should be solely competent to decide on all disputes concerning the

¹ 4A_18/2007, available online at: www.bger.ch. See also the comments contributed by Tavenier Tschanz, Supreme Court Clarifies Pre-Arbitration Conciliation Requirement, in: International Law Office Newsletter of September 6, 2007, online at: <http://www.internationallawoffice.com/Newsletters>.

² So-called "Med-Arb clauses", see HOCHSTRASSER|BLESSING, in: Honsell|Vogt|Schyder|Berti (eds.), Internationales Privatrecht, 2nd ed., Basel 2007, Einleitung zum Zwölften Kapitel: Grundlagen, N 329; PETER, Med-Arb in International Arbitration, in: American Review of International Arbitration (ARIA) 1997, Vol. 8. No. 1., pp. 83-116; BUEHRING-UHLE, Co-Med-Arb Technique Holds Promise for Getting Best of Both Worlds, 2006 Juris Net. Such clauses are also titled "multi-tiered" or "ADR-first" or "escalation" clauses. See BERGER, Law and Practice of Escalation Clauses, in: Arbitration International, Vol. 22 No. 1 (2006), pp. 1-17, p. 1.

³ Clause 10.2: "Toute controverse et tout différend en rapport avec le présent contrat et qui ne pourront être résolus à l'amiable (y compris la conciliation selon les règles de l'OMPI) devront être soumis à un tribunal arbitral qui sera seul compétent pour décider définitivement, à l'exclusion des tribunaux ordinaires. Au surplus, le tribunal arbitral sera seul compétent pour statuer sur tout différend concernant l'applicabilité de cette clause d'arbitrage. Des négociations en cours ne constitueront en aucun cas un empêchement à l'engagement de la procédure arbitrale."

⁴ World Intellectual Property Organization, www.wipo.int.

applicability of this arbitration clause. The clause continued that ongoing negotiations should not constitute an impediment for engaging in arbitration proceedings.

II. Importance of the Question

The question of whether the arbitral tribunal's jurisdiction is affected by an agreement to try to settle the dispute by means of mediation first is of crucial importance.

As Professor Berger has put it, such clauses bear a particular risk of being pathological and, hence, inoperable for an arbitral tribunal.⁵ This could lead to the result that the parties' former intention could be frustrated. When dispute already arose, it could be impossible to agree on another non-pathological clause.

Additionally, in the case of pathological clauses, besides different courts or arbitral tribunals possibly being competent to decide on the meaning of the clause and, hence, on their jurisdiction, different courts could be competent to hear the merits of the case.

Furthermore, issues regarding periods of limitations may arise. For example, it could be impossible to interrupt running periods of limitations during the mediation process and the claimant's claim could become time-barred while the parties' dispute-resolution process has already been initiated.

Moreover, in some rare cases, the normative interpretation of the mediation-arbitration clause might entitle one party to avoid the arbitration agreement. This could then lead to inefficiency or even greater procedural problems.

Additionally, if the arbitral tribunal accepts its jurisdiction, the award might later be challenged.

A. The Parties' Possibility to Define the Arbitral Tribunal's Jurisdiction

The problem resulting from unclear clauses is that an arbitral tribunal will cautiously avoid that its award will later be set aside because of its lack of

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BERGER, op. cit., p. 1.

jurisdiction. It is one of the arbitral tribunal's primary duties to render an enforceable award.⁶

The parties, namely, can limit an arbitral tribunal's jurisdiction in various ways. This will of the parties defines the frame of the arbitral tribunal's competence.

The scope of the arbitration agreement can be limited to specific material questions. It could also, for example, be limited with respect to time.⁷ The parties can subject the effectiveness of the arbitration agreement to various precedent⁸ or resolutive⁹ conditions.¹⁰ The validity of the arbitration agreement in such events is to be determined by the arbitral tribunal¹¹ by applying either¹² the law chosen by the parties, the law governing the dispute or Swiss law, as the case may be (Article 178 para. 2 PILA).

1. Conditional Arbitration Agreements

If Swiss law applies, as was the case in the decision of the Swiss Federal Tribunal presented in the beginning, Article 151 and the following articles of the

⁶ See HORVATH, The Duty of the Tribunal to Render an Enforceable Award, J. Int'l Arb. Vol. 18/2 (2001), pp. 135–158, for more information regarding this duty.

⁷ In a case decided by the Federal Tribunal in 1995, the parties agreed that the dispute be submitted to an arbitral tribunal within a time limit of 30 days. The Federal Tribunal found that this means that the parties wanted to exclude the arbitral tribunal's jurisdiction after the expiry of this time limit. See Federal Tribunal, decision of 17 August 1995, in: ASA Bulletin 1996, p. 678-679.

⁸ German: "Suspensivbedingungen" (CO) or "auflösende Bedingungen" (German BGB). For the example of mediation proceedings as a possible condition precedent to arbitration agreements, see RÜEDE|HADENFELDT, op. cit., p. 194 at footnote 456. See also HIM Portland v. DeVito Builders, Inc., No. 02-1955 (1st Cir. Jan. 17, 2003), Dispute Resolution Journal, Feb-Apr 2003, summarized online at: http://findarticles.com/p/articles/mi_qa3923/is_200302/ai_n9225817. Online at: http://caselaw.lp.findlaw.com/scripts/prINTER_friendly.pl?page=1st/021955.html.

⁹ German: "Resolutivbedingungen".

¹⁰ See RÜEDE|HADENFELDT, Schweizerisches Schiedsgerichtsrecht, 2nd ed., Zurich 1993, p. 59.

¹¹ Doctrine of (relative) Competence-Competence (Article 186 para. 1 PILA). Cf. DFC 128 III 50, p. 59 et seq. The doctrine of Competence-Competence, i.e., the arbitral tribunal's power to decide on its own competence to hear the dispute, is "relative", because it only applies vis-à-vis a regular state court (and other tribunals). The control of the arbitral tribunal's decision by the Federal Tribunal (Article 190 para. 2 lit. b PILA) is not affected by this doctrine.

¹² Alternatively. If it is valid under one of these laws, the arbitration agreement is accepted to be valid. See WENGER|MÜLLER, in: Honse|Vogt|Schyder|Berti (eds.), op. cit., Art. 178 N 24.

Swiss Code of Obligations (**CO**) apply with regard to conditions to which the arbitration agreement possibly is subject.

The very moment the condition is fulfilled, the validity of a clause that was subject to a condition commences (Article 151 para. 2 CO). In other words, if the parties introduced mediation as a condition precedent, there is no valid arbitration agreement before the mediation ended unsuccessfully.

Whether or not the parties actually wanted to suspend the effectiveness of the arbitration agreement, is to be answered by means of interpretation of the contract.

2. Interpreting the Arbitration Agreement

a) The Arbitrator's or Judge's Approach of Establishing the Parties' Will

In order to establish the content of an agreement, the parties' true will is relevant (Article 18 para. 1 CO).¹³ The wording of the parties' respective declarations serves as a starting point.¹⁴ The respective party's behaviour after the conclusion of the contract, as well as other elements such as business practices are also relevant.¹⁵ When the true will of each party is established, it is decisive whether there was a meeting of the parties' minds.¹⁶ If, after this first phase of interpretation, it is obvious that the parties had a corresponding will, the contract had been concluded with the respective content.¹⁷

If, however, the true will of the parties differs, or is unascertainable in the first place - as is the case with unclear mediation-arbitration clauses -, the question of the meeting of the minds and, hence, the content of a contract is to be

¹³ KRAMER, Berner Kommentar, VI|1|1, Bern 1986, Art. 18 N 21.

¹⁴ KRAMER, op. cit., Art. 18 N 22.

¹⁵ KRAMER, op. cit., Art. 18 N 28, 29.

¹⁶ KRAMER, op. cit., Art. 18 N 21.

¹⁷ The situation where there was no meeting of the minds and where the parties knew about this fact is also unproblematic. See KRAMER, op. cit., Art. 18 N 67. In this case, no contract was concluded - or, in the present context, no condition precedent or resolutive introduced with regard to the effectiveness of the arbitration agreement.

established by objective elements based on principles of reliance.¹⁸ Here, all circumstances of the case, including the wording of the declarations and business practices etc., must again be taken into account.¹⁹ The approach, however, is principally different. The arbitrator does not try to establish the true will of the parties at this stage but rather asks whether the recipient of the declaration correctly interpreted the indications of the other party's true will under the circumstances of the conclusion of the respective contract.²⁰ If a reasonable recipient of the other party's declaration standing in the shoes of the actual recipient would have been entitled to and in fact would have had to understand it the way it was understood, this understanding is relevant.²¹

With regard to the question of the effectiveness of an arbitration agreement before the unsuccessful effort to solve the dispute by means of mediation, this procedure also is the correct approach.²²

b) The Parties' Possibility to Clarify Their Will

This interpretation by the arbitrators or judges entails a certain risk of an interpretation that is not in favour of one party. But, the parties have the possibility to limit the arbitrators' or judges' possibility to interpret their agreement. This would enhance their legal certainty and the predictability, for example, with regard to costs or the length of the settlement of their dispute.

Wording such as "the parties may refer to mediation", should make it sufficiently clear that mediation is a mere voluntary option before initiating arbitration

¹⁸ DFC 125 III 305, p. 308; KRAMER, op. cit., Art. 18 N 67; SCHWENZER, Schweizerisches Obligationenrecht Allgemeiner Teil, 4th ed., Bern 2006, N 27.40.

¹⁹ Cf. DFC 116 II 695, p. 696; DFC 120 II 182, p. 184; KRAMER, op. cit., Art. 18 N 71; SCHWENZER, op. cit., N 27.35. For details regarding interpretation, see KRAMER, op. cit., Art. 18 N 22 et seq.

²⁰ KRAMER, op. cit., Art. 18 N 71. Such an interpreted declaration of a party's will is called a "normative declaration of will", see SCHWENZER, op. cit., N 27.41.

²¹ DFC 125 III 305, p. 308; SCHWENZER, op. cit., N 27.41.

²² Federal Tribunal, 4P.253/2003, decision of 25 March 2004, at 5.3.; BERGER, op. cit., p. 3.

proceedings.²³ Wording such as "shall refer to mediation first", in contrast, suggests a mandatory mediation process before arbitration.²⁴

If the parties indeed want mediation before arbitration, they should also mention a specific set of rules governing the mediation and/or mention a particular institution administering it.

Moreover, the parties should clarify within which time frame they want to try that their dispute is successfully solved by mediation. In the case decided by the Federal Tribunal mentioned in the beginning, namely, the Federal Tribunal stated that this serves as an indicator that the mediation proceedings are meant to be mandatory before arbitration.²⁵ This factor, in the Federal Tribunal's view, is relevant because it is common practice to do this when the parties actually want to first settle their dispute amicably before submitting it to an arbitral tribunal.

Whatever mechanism the parties prefer, they should discuss this issue in the drafting process and choose a wording that reflects their common will in the best way possible.

B. Recognition of the Arbitration Agreement

When discussing the issue of how the arbitration agreement is interpreted, the question of who is competent to interpret it immediately arises.

Problems (e.g. conflicting decisions or a deadlock because neither the court nor the tribunal accepts its jurisdiction) could arise if one party initiates arbitration proceedings and the other party simultaneously submits the case to a national court. Depending on the procedural rules of the respective court, it could be competent to decide on the validity of the arbitration agreement.²⁶ The New York Convention does not know a priority rule (i.e., that in the case of two pending parallel proceedings the arbitral tribunal's competence takes precedence over

²³ BERGER, op. cit., p. 4.

²⁴ BERGER, op. cit., p. 4.

²⁵ Federal Tribunal, 4A_18/2007, decision of 6 June 2007.

²⁶ See ARROYO, *Lis Pendens in International Arbitration - The Newly Adopted Swiss Approach*, in: *Stockholm International Arbitration Review* 2007:1, pp. 19-39, p. 23 et seq.

the court's competence), either.²⁷ In Switzerland's newly²⁸ amended arbitration law, the arbitral tribunal fortunately does not have to stay the proceedings and is still competent to decide on its jurisdiction regardless of the claim already being pending before a state court or another arbitral tribunal, unless serious reasons require it (Article 186 para. 1^{bis} PILA). If the arbitral tribunal issues an interim award on jurisdiction, the national court would no longer be competent to decide on this question because of the principle of *res iudicata*.

Still, this uncertainty could lead to procedural inefficiency or, in the worst case, lead to the result that the national court is competent and materially decide on the issue instead of an arbitral tribunal.²⁹

Similar problems exist with respect to the competence to hear and decide the merits of the dispute.

While in member states³⁰ of the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitral Awards (**NYC**) arbitration agreements are generally recognized (Article II NYC) and, hence, no ordinary court could assume competence while there are ongoing voluntary mediation proceedings but an arbitration agreement exists, the situation could be different with regard to mandatory mediation proceedings.

While the problem is not new with regard to jurisdiction of national courts not recognizing arbitration agreements at all - because then simple arbitration agreements would not be recognized, either -, some jurisdictions possibly could distinguish between normal arbitration agreements and such arbitration agreements that are subject to a condition precedent and, thus, theoretically not in effect, yet.

²⁷ ARROYO, op. cit., p. 32.

²⁸ March 1, 2007.

²⁹ In Germany, the possibility of court and arbitral proceedings would be suspended. See BERGER, op. cit., p. 5.

³⁰ Currently 142 Member States, see online at: http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/NYConvention_status.html (last accessed: 12 October 2007).

For example, in the case *HIM Portland v. DeVito Builders*³¹ decided by the United States Court of Appeals regarding a decision of the District Court of Maine in 2003, the parties agreed that "Claims [...] arising out of or relating to this Contract [...] shall be referred initially to the Architect for decision. Such matters [...] shall, after initial decision by the Architect, or 30 days after submission of the matter to the Architect, be subject to mediation as a condition precedent to arbitration or the institution of legal or equitable proceedings by either party". The district court had denied HIM's motion to compel arbitration. HIM appealed, claiming that because the contract required arbitration, but not mediation, the court should have compelled arbitration. The Court of Appeals disagreed and stated: "under the plain language of the contract, the arbitration provision [...] is not triggered until one of the parties requests mediation." It continued: "[i]t is difficult to imagine language which more plainly states that the parties intended to establish mediation as a condition precedent to arbitration proceedings." The Court of Appeals generally stated that "arbitration is a matter of contract law and consequently a party cannot be required to submit to arbitration any dispute which he has not agreed so to submit". It further held that "the F[ederal] A[rbitration] A[ct]'s proarbitration policy does not operate without regard to the wishes of the contracting parties".

In this case, the Court left open the question of whether mediation is a condition precedent to bring suit at all (i.e., before a national court or before an arbitral tribunal), because the parties had not raised this issue. ADR-first clauses, namely, could indeed be regarded as a waiver of the possibility to sue before a court or tribunal before amicable dispute resolution has not taken place.³² Some jurisdictions regard such agreements as being procedural law agreement.³³ In Switzerland, however, the Court of Cassation in Zurich³⁴ has ruled that agreements not to sue (*pactum de non petendo*) are no procedural requirement but merely a question of substantial law and, hence, an action before a court is not to be dismissed as inadmissible. Rather, the claiming party risks that the claim is rejected for substantial reasons. The Federal Tribunal rejected an appeal

³¹ *HIM Portland v. DeVito Builders, Inc.*, No. 02-1955 (1st Cir., Jan. 17, 2003), see online at: http://caselaw.lp.findlaw.com/scripts/printer_friendly.pl?page=1st/021955.html.

³² BERGER, op. cit., p. 5, with references e.g. to Germany and England, stating that, dogmatically, this could be regarded a *pactum de non petendo*. For Swiss law, see E.J. HABSCHEID, op. cit., p. 943.

³³ BERGER, op. cit., p. 5.

³⁴ See Kassationsgericht Zürich, decision of 15 March 1999, in ASA Bulletin 2002, pp. 373-376, p. 374.

against this decision.³⁵ Authors discussing it criticized the Court of Cassation's decision.³⁶

The same problems could arise in an arbitration proceeding. An arbitral tribunal could, by exercising its competence-competence, come to the conclusion that it is not yet competent to hear the dispute because the effectiveness of the arbitration proceeding is suspended by the condition or it could reject the claim (temporarily or finally,³⁷ as the case may be). Authors suggest that in the optimal case, arbitration proceedings should be validly initiated but then immediately suspended.³⁸ In their view, arbitrators should - e.g. by means of a procedural order - set a time limit for the suspension.³⁹ This allows the party relying on the mediation requirement to initiate such proceedings appropriately while simultaneously minimizing the risk of procedural inefficiency and of a limitation of the claim.

In the case before the Swiss Federal Tribunal illustrated above, the Federal Tribunal mentioned that it could even be against good faith⁴⁰ to rely on the two-step mechanism while never instituting mediation proceedings itself.⁴¹ In Swiss law, the obvious abuse of rights is not protected (Article 2 para. 2 Civil Code).

Bearing these problems in mind, the parties should check whether such a particular problem exists with regard to any jurisdiction involved and act accordingly (e.g., refrain from incorporating a two-step mechanism or sufficiently clarify their will).

³⁵ Federal Tribunal, decision of 23 August 1999, mentioned in ASA Bulletin 2002, p. 375.

³⁶ See VOSER, Sanktionen bei Nichterfüllung einer Schlichtungsklausel - 15. März 1999 - Kassationsgericht Zürich, in: ASA Bulletin 2002, pp. 376-381; BERGER, op. cit., p. 6.

³⁷ WENGER|SCHOTT, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 186 N 23, stating that the arbitral tribunal could finally dismiss the claim if the condition precedent cannot be fulfilled. In Swiss law, however, according to Article 156 CO, a condition is deemed to be fulfilled (Art. 151 para. 2 CO) if one party acting in bad faith has prevented its occurrence.

³⁸ VOSER, op. cit., p. 379; WENGER|SCHOTT, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 186 N 23.

³⁹ See VOSER, op. cit., p. 379.

⁴⁰ Because of contradictory behaviour ("venire contra factum proprium").

⁴¹ Federal Tribunal, 4A_18/2007, decision of 6 June 2007, at 4.3.3. See also BERGER, op. cit., p. 14, stating that a party that has not initiated or even refused to participate in mediation cannot rely on this argument because of estoppel by conduct.

C. Possibility to Interrupt Periods of Limitation

Another important issue that mediation-arbitration clauses could raise is their effect on the parties' possibility to interrupt running periods⁴² of limitation.

Depending on the applicable law, namely, only initiating proceedings before a state court or initiating arbitration proceedings or initiating debt collection proceedings interrupt periods of limitations.⁴³

If the parties agreed on a mediation-arbitration procedure - and mediation is considered to be a condition precedent in the specific case - an arbitral tribunal would not be competent to hear the dispute, yet. In some cases, this could lead to the limitation of the claimant's claim during a mediation proceeding.

To avoid this consequence, the parties to mediation-arbitration clauses should stipulate that mediation - despite being required before arbitration - does not have the effect that arbitration proceedings could not validly be initiated. Rather, the parties should provide that the arbitrators would have to suspend the arbitration proceedings so long as there are mediation proceedings going on that have not unsuccessfully ended (in accordance with the applicable rules).

Alternatively, the parties should, as was suggested by the Swiss Federal Tribunal in the case mentioned in the beginning,⁴⁴ implement periods within which mediation procedures should be initiated and successfully completed. In addition to serving as an indicator that the mediation proceedings are meant to be mandatory before arbitration, it serves the purpose to prevent the opposing party to unduly prolong and delay the dispute resolution process.⁴⁵

⁴² For an article discussing the proper limitation regime in international sales contracts in international arbitration, see SCHWENZER|MANNER, 'The Claim is Time-Barred': The Proper Limitation Regime for International Sales Contracts in International Commercial Arbitration, in: *Arbitration International*, Vol. 23 No. 2 (2007), pp. 293-307.

⁴³ For Switzerland, see E.J. HABSCHIED, *Die aussergerichtliche Vermittlung (Mediation) als Rechtsverhältnis*, in: *AJP/PJA* 2001 pp. 938-944, p. 943.

⁴⁴ Federal Tribunal, 4A_18/2007, decision of 6 June 2007.

⁴⁵ Also see SCHUMACHER, *Vertragsgestaltung, Systemtechnik für die Praxis*, Zurich 2004, p. 115.

D. Danger of Avoidance of the Arbitration Agreement

Another problem is that if - after interpretation - it is established by the arbitral tribunal that the parties' minds actually never met but that only, based on principles of reliance, the objectified normative interpretation of the parties' respective declaration of will leads to the result that one party is bound to the objective understanding of its declaration, this party might avoid the arbitration clause itself. By doing this, it could possibly indirectly challenge the award.

1. Possible Grounds for Avoidance and the Requirements for it

If one party's will does not conform to the objective understanding of its declaration, an error with regard to this declaration (so-called "Erklärungsirrtum") could be at hand.⁴⁶ Although an error regarding the question of whether the parties first wanted to mediate and only then to arbitrate is not covered by the cases set forth in Article 24 Ciff. 1.-3. CO, where the essentiality of the error - a necessary prerequisite in order to allow a party to avoid a contract (Article 23 CO) - is assumed, this list is not exhaustive.⁴⁷

If, in the specific case, a party could actually show that the error was both subjectively and objectively essential, it could theoretically avoid the arbitration agreement. If the party - after the arbitral tribunal stated that a normative objective understanding of its declaration of will does not require mediation before arbitration - indeed avoids the arbitration agreement before or shortly⁴⁸ after an award was issued, this agreement falls away.

It is somehow unlikely that the Federal Tribunal would actually follow the avoiding party's arguments that performing mediation actually was so essential to it that it only consented to waive the competence of the ordinary courts for the

⁴⁶ An error in declaration ("Erklärungsirrtum") in form of an error regarding the content of the declaration ("Inhaltsirrtum") is at hand if the declaring party wanted the declaration but attached a different meaning to it. See SCHWENZER, op. cit., N 37.09.

⁴⁷ Although no cases exist where the essential nature of an error was accepted in cases not set forth in Art. 24 Ciff. 1.-3. CO. See SCHWENZER, in: Honsell|Vogt|Wiegand (eds.), Obligationenrecht I: Art. 1-529 OR, 4th ed., Basel 2007, Art. 24 N 1.

⁴⁸ The period within which avoidance for reasons or an error is possible under Swiss law is 1 year after the party's knowledge that it erred, Article 31 CO.

rare⁴⁹ event that mediation was not successful. By showing the will to submit their dispute to mediation and then to arbitration, the parties unambiguously showed their will to waive the competence of ordinary state courts. This is true for both cases, where the parties wanted a two-step approach or just an option to try mediation before arbitration. But the risk still exists.

2. Effects of a Successful Avoidance of the Agreement to Arbitrate

Despite the fact that a successful avoidance of the arbitration agreement because of an error is unlikely, in the following, the consequences of a successful avoidance will be discussed.

In normal situations, avoiding a contract because of error has a retroactive (ex tunc) effect. That means that the contract is considered to never have existed.⁵⁰ The only exception to this rule exists in cases of contracts for the performance of a continuing obligation ("Dauerschuldverhältnisse"). In these cases, the contract does not retroactively fall away but the avoidance only affects the future of the contract (ex nunc).⁵¹

The effect of a hypothetical avoidance of the arbitration agreement because of one party's error in declaration, hence, depends on the question of qualifying the arbitration agreement as a continuous obligation.

An arbitration agreement is not limited to a single exchange of performances. This would indeed qualify it as a continuing obligation. This view seems to also be advanced in legal literature. Some authors rely on the rules governing continuous obligations contracts when arguing in connection with a party's right to terminate the arbitration agreement.⁵² They argue that the parties to an arbitration agreement - independent from the question of whether it is a contract

⁴⁹ According to some statistics, mediation is very successful. See, for example, the statistics of CMAP - Centre de Médiation et d'Arbitrage de Paris, online at: <http://www.mediationetarbitrage.com>, showing that 71% of all its efforts to solve disputes by mediation, ended successfully. According to other sources, almost 80% of all cases submitted to mediation result in a settlement. See Mediation Seen as Highly Effective ADR Process, 2006 Juris Net.

⁵⁰ SCHWENZER, op. cit., N 39.23.

⁵¹ DFC 129 III 320, p. 328 et seq.; SCHWENZER, op. cit., N 39.25.

⁵² See WENGER|MÜLLER, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 178 N 85; RÜEDE|HADENFELDT, op. cit., p.103.

of material or procedural law⁵³ - form some kind of procedural partnership.⁵⁴ Other authors hold a different view but also state that the rules of continuous obligation contracts must be applied in analogy.⁵⁵

The consequence of this qualification - or at least the analogous application of the rules - is that any avoidance of the arbitration agreement because of an error does not retroactively affect the validity of the arbitration agreement on which the arbitral tribunal based its competence.⁵⁶ Only in case of future disputes, the parties could no longer rely on the lapsed arbitration agreement but would have to go in front of the competent court in order to settle their dispute or would have to conclude a new arbitration agreement.

E. Danger that the Award May be Challenged

In Switzerland, the 12th chapter of the Swiss Private International Law Act (**PILA**) applies as *lex arbitri* if the arbitral tribunal's seat is within Switzerland and at least one party did not have its place of business within Switzerland at the time of the conclusion of the arbitration agreement (Article 176 para. 1 PILA). Hence, if one party challenges an award by an arbitral tribunal sitting in Switzerland, Articles 190 to 192 PILA apply. These articles limit the grounds for challenge to specific issues.

In Switzerland, the award may be set aside only for one of the following (exhaustive)⁵⁷ reasons: First, if the sole arbitrator or the tribunal, respectively, was constituted in an irregular way. Second, if the arbitral tribunal wrongfully accepted or declined jurisdiction.⁵⁸ Third, if the arbitral tribunal decided on points

⁵³ For this discussion see HABSCHEID (and Berti), *Schweizerisches Zivilprozess- und Gerichtsorganisationsrecht*, 2nd ed. Basel 1990, p. 515 et seq.

⁵⁴ HABSCHEID (and Berti), *op. cit.*, p. 516.

⁵⁵ RÜEDE|HADENFELDT, *op. cit.*, p. 197, N 669.

⁵⁶ See also RÜEDE|HADENFELDT, *op. cit.*, p.104, stating that the validity of a final and effective award is not affected by a subsequent forfeiture or termination of the arbitration agreement on which it is based.

⁵⁷ DFC 119 II 380, p. 383; Federal Tribunal, 4P.208/2004, decision of 14 December 2004, at 3.1.; Federal Tribunal, 4A.17/2007, decision of 8 June 2007, at 3.2.; MÜLLER, *op. cit.*, p. 142; BERTI|SCHNYDER, in: Honsell|Vogt|Schyder|Berti (eds.), *op. cit.*, Art. 190 N 24.

⁵⁸ This includes cases where the arbitral tribunal assumed jurisdiction regarding issues not covered by the arbitration agreement. BERTI|SCHNYDER, in: Honsell|Vogt|Schyder|Berti (eds.), *op. cit.*, Art. 190 N 38, 53.

of dispute that were not submitted to it (*ultra petita*) or if the arbitral tribunal left prayers for relief undecided which were correctly submitted to it (*infra petita*).⁵⁹ Fourth, if the principle of equal treatment of the parties or the right to be heard was violated. Finally, the award may be set aside if it is incompatible with Switzerland's public policy, i.e. if it violates fundamental rules of law.⁶⁰

1. Waiver of the Possibility to Challenge

The parties may think of waiving the possibility to challenge the award. This, however, is only possible in certain cases and specific requirements must be respected.

a) No Place of Business in Switzerland

First, a waiver is only possible if none of the parties has its domicile, ordinary residence or a business establishment in Switzerland. The negative requirement of the absence of a business establishment in Switzerland even frustrates a waiver if one of the parties merely has a branch in Switzerland that, however, is in no way involved in the dispute.⁶¹ If one of the parties has a Swiss subsidiary that is not involved in the dispute at all, the waiver is admissible.⁶² Hence, such a waiver is not possible in all cases.

b) Express Waiver of Particular Appeal Required

If a waiver of the possibility to challenge the award is possible, the parties must agree on the waiver of the right to challenge the award either by an explicit

⁵⁹ BERTI|SCHNYDER, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 190 N 53.

⁶⁰ E.g. the principle of *pacta sunt servanda*. This principle is violated if the arbitral tribunal, for example, acknowledges the existence of a contract but disregards the consequences arising therefrom. Cf. BERTI|SCHNYDER, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 190 N 74; HEINI, in: Zürcher Kommentar zum IPRG, 2nd ed., Zurich 2004, Art. 190 N 45.

⁶¹ PATOCCHI|JERMINI, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 192 N 4 et seq.; MÜLLER, International Arbitration: A Guide to the Complete Swiss Case Law (Reported and Unreported), Zurich 2004, p. 10.

⁶² PATOCCHI|JERMINI, op. cit., Art. 192 N 5. The reason for this is that the subsidiary is legally independent.

agreement in the written arbitration agreement or in another written⁶³ subsequent agreement (Article 192 para. 1 PILA).⁶⁴

An agreement that the arbitral tribunal should definitively decide on the subject matter of the dispute, with the exclusion of ordinary courts, expresses no will of the parties to waive any possibilities to challenge the award in front of the Federal Tribunal. It is not sufficient to globally waive the possibility to appeal the award, either. The parties must clearly state the right of appeal they want to waive and actually waive it.⁶⁵

If the parties indeed want to waive the possibility of challenge, the parties, for example, could state in the respective arbitration agreement: "The parties explicitly waive the possibility to challenge the arbitral tribunal's award within the meaning of Article 192 of the Swiss Private International Law Act of December 18, 1987, as amended".

c) **No Possibility of Waiver by Reference**

The parties drafting their contract might think that the reference to a set of rules providing for the waiver of the possibility to challenge the award is sufficient. The WIPO Rules, for example, to which the parties referred in the case discussed in the beginning, state that "[b]y agreeing to arbitration under these Rules, the parties undertake to carry out the award without delay, and waive their right to any form of appeal or recourse to a court of law or other judicial authority, insofar as such waiver may validly be made under the applicable law" (Article 64, Effect of the Award).

But in Swiss arbitration law, indirect waivers, i.e., if the waiver of the right to appeal the award is only set forth in the rules of arbitration, are not sufficient.⁶⁶

⁶³ The term "written" is to be understood within the meaning of Article 178 para. 1 PILA, i.e., means of communication that allow proof of the agreement by text. See PATOCCHI|JERMINI, op. cit., Art. 192 N 13.

⁶⁴ According to a recent decision by the Federal Tribunal, the written consent to waive the possibility to challenge the award is invalid, if it is not based on the free will of both parties. This will could, in the specific case, be limited if there are exceptional circumstances, such as, for example, a strict hierarchy and imbalance of power between an athlete and a sports organization. See DFC 133 III 235, p. 242, at 4.3.2.2.

⁶⁵ DFC 116 II 639, p. 640.

⁶⁶ DFC 116 II 639, p. 640; Federal Tribunal, 4P.62/2004, decision of 1 December 2004, at 1.2.

This is true even in cases where the rules themselves do not acknowledge this fact, as do the WIPO Rules by stating "insofar as such waiver may validly be made under the applicable law". In the case before the Federal Tribunal mentioned above, the Federal Tribunal accordingly correctly rejected the existence of a waiver.

Consequently, parties who agree that there should be no possibility to challenge an award rendered by the arbitral tribunal should clearly state so in their arbitration agreement. This would not be a mere restatement of the arbitration rules agreed upon by the parties but rather safeguards the validity of the waiver when the place of arbitration is in Switzerland.

2. Wrongful Acceptance of Jurisdiction by an Arbitral Tribunal and the Federal Tribunal's Cognizance

If there is no (valid) waiver by the parties with regard to the possibility to set aside the award, the alleged lack of jurisdiction (Article 190 para. 2 lit. b. PILA) is of primary importance in the context of pre-arbitral mediation or conciliation mechanisms agreed upon by the parties.

As we have seen above, ambiguous clauses require the interpretation by the arbitral tribunal or the court, as the case may be.

If the interpretation leads to the normative result that the correct understanding would have been that a two-step approach was not objectively intended by the parties, the arbitration agreement is not subject to a condition precedent and, hence, valid from the moment of its conclusion. The consequence then would be that the award would not have to be set aside.

If, however, the parties normatively agreed on a two-step approach - i.e., first mediate, and then arbitrate - the arbitral tribunal had no jurisdiction to hear the dispute, yet. In this case, either the arbitral tribunal rejected its jurisdiction in the first place, or if the arbitral tribunal assumed jurisdiction nevertheless, any award could be set aside.

The party that argued against the possibility to initiate arbitration proceedings where there was no mediation beforehand could accordingly think that it simply refers the question of the validity of the arbitration agreement to the Federal Tribunal. This party could expect that the Federal Tribunal comes to a different conclusion and sets aside the award because of lack of jurisdiction.

If the parties' consent to arbitrate was not based on the actual will⁶⁷ but on the objective normative interpretation of the parties' declaration by the arbitral tribunal, this indeed is a legal question that could be verified by the Federal Tribunal in the context of Art. 190 para. 2 lit. b PILA.⁶⁸

The challenging party, however, should lower its expectations with regard to the success of the challenge. The arbitral tribunal, namely, based its decision on the facts of the specific case.

An appeal to the Swiss Federal Tribunal regarding an award by an arbitral tribunal, in general,⁶⁹ is governed by the same rules as an appeal against a decision by one of the highest cantonal courts (Article 191 PILA and Article 77 of the Act on the Federal Tribunal, **FTA**).

Theoretically, the Federal Tribunal is free to legally verify the competence of the arbitral tribunal - including preliminary questions of material law.⁷⁰ But, the Federal Tribunal is principally bound by the facts on which the arbitral tribunal based its decision (Article 105 FTA), unless these facts are the issue of the appeal or new facts exist.⁷¹ The result of this limited competence of the Federal Tribunal is that it will be unlikely that it comes to a different conclusion with regard to the interpretation of the arbitration agreement than the arbitral tribunal did.

⁶⁷ Which would then be a fact established by the arbitral tribunal on which the Federal Tribunal is principally bound. Federal Tribunal, 4P.253/2003, decision of 25 March 2004, at 5.3.

⁶⁸ Federal Tribunal, 4P.253/2003, decision of 25 March 2004, at 5.3.

⁶⁹ Only in accordance with Articles 190-192 PILA and with other differences, e.g. regarding the Federal Tribunal's possibility to decide on the merits of the case.

⁷⁰ Federal Tribunal, 4P.253/2003, decision of 25 March 2004, at 4.2.; BERTI|SCHNYDER, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 190 N 36.

⁷¹ Federal Tribunal, 4A_42/2007, decision of 13 July 2007 ("*Das Bundesgericht prüft die Zuständigkeitsrüge nach Art. 190 Abs. 2 lit. b IPRG in rechtlicher Hinsicht frei, einschliesslich materiellrechtliche Vorfragen, von deren Beantwortung die Zuständigkeit abhängt. Allerdings überprüft das Bundesgericht die tatsächlichen Feststellungen des angefochtenen Schiedsentscheids auch im Rahmen der Zuständigkeitsrüge nur, wenn gegenüber diesen Sachverhaltsfeststellungen zulässige Rügen im Sinne von Art. 190 Abs. 2 IPRG vorgebracht oder ausnahmsweise Noven berücksichtigt werden*"). For previous decisions, see DFC 133 III 139, p. 141; DFC 129 III 727, p. 733. See also SEILER|WERDT|GÜNGERICH, Bundesgerichtsgesetz (BGG), Bern 2007, Art. 77 N 8; BERTI|SCHNYDER, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 190 N 51; HEINI, in: Zürcher Kommentar zum IPRG, op. cit., Art. 191 N 14.

It seems surprising that the Swiss Federal Tribunal's cognizance is that limited. However, it was an intentional decision by the legislator to limit the Swiss Federal Tribunal's competence regarding decisions by arbitral tribunals in international arbitration.⁷² Moreover, it is in line with the general principle of competence-competence and the intentionally limited possibility to verify the arbitrators' decision associated with it.

III. Insides Gained

From the discussion above, certain lessons can be learned.

The parties' incorporation of mediation-arbitration clauses in their contracts raises additional problems and uncertainties. The parties, however, can deal with these problems.

Hence, parties should clearly state whether they only want arbitration in case of an unsuccessful attempt to mediate or whether it is a mere voluntary option. Preferably, the parties should provide periods within which mediation must be initiated (and in accordance with which rules) and the time frame for finding a possible amicable resolution to their dispute.

Additionally, if the parties agree on a mandatory two-step approach, they should carefully contemplate the problems that such a mechanism could create, e.g. with regard to limitation periods or jurisdiction of other courts. Once they have contemplated these problems, they should decide on them and proactively state their common will.

If both parties have their place of business outside of Switzerland, they could waive the possibility to challenge the award in front of the Federal Tribunal by express wording in the written arbitration clause.

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Dr. iur. Benjamin Leisinger

⁷²

BERTI|SCHNYDER, in: Honsell|Vogt|Schyder|Berti (eds.), op. cit., Art. 190 N 24.